

205773

## Report of Independent Accountants on Applying Agreed-Upon Procedures

The Board of Directors and Management  
Continental Airlines, Inc.  
and  
The Federal Aviation Administration

FAA-02-13918-13

We have performed the procedures enumerated below, which were agreed to by Continental Airlines, Inc. (Continental Airlines or the Company) and the Federal Aviation Administration (FAA), solely to assist you in evaluating the accompanying schedule of incremental costs directly associated with Passenger Facility Charges (PFC) collection, handling, remittance, reporting, recordkeeping, and auditing for the year ended December 31, 1999. These incremental costs are included in the Continental Airlines, Inc. Summary Schedule (the Schedule) under the caption "Actual Costs 1999," included as an Exhibit. Our procedures do not extend to other information (except as noted in step 6 below) included in the Schedule. This engagement to apply agreed-upon procedures was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the FAA and the Company. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

It should be understood that certain of the schedules and/or analyses provided to us by the Company calculated incremental costs directly associated with PFCs based on assumptions and/or studies performed by the Company. Accordingly, we make no comment as to the reasonableness of the assumptions or as to the methodology underlying the studies.

The following procedures were performed without any exceptions noted:

1. We obtained the Schedule from the Company of all costs attributed to the collection and administration of PFCs, by expense caption, for the year ended December 31, 1999.



2. We obtained a schedule from the Company of the total dollar amount of PFCs collected, refunded, and remitted for the year ended December 31, 1999, and agreed the total to a Continental Airlines system-generated report. We recalculated the number of PFCs collected for the year by dividing the total dollar amount of PFCs collected by \$3.
3. We obtained a schedule from the Company of the total dollar amount of interest revenue earned by the Company on PFC funds it held from the time of collection from passengers to the time of remittance to the airports (or the refund of the PFC funds to passengers) for the year ended December 31, 1999.
4. We recalculated the summation of the "Total Costs" under the caption "Actual Costs 1999", as reported on the Schedule obtained in step 1., for clerical accuracy.
5. We performed the following procedures related to each expense caption, as listed on the Schedule obtained in step 1., and the interest revenue amount as reported on the schedule obtained in step 3., for the year ended December 31, 1999:

Cost CaptionProcedures

- |                     |  |
|---------------------|--|
| a. Credit Card Fees | <ol style="list-style-type: none"><li>i. We obtained from the Company a schedule containing the breakout of total sales by month, for the year ended December 31, 1999, separated between cash sales and credit card sales, and agreed two months of credit card sales (April 1999 and October 1999) to the general ledger.</li><li>ii. We recalculated, based on the schedule obtained in step 5.a.i., the percentage of credit card sales as a portion of total sales for the year.</li><li>iii. We recalculated "PFC dollars collected via credit card sales" for the year ended December 31, 1999, by multiplying total PFC dollars collected less PFC dollars refunded, from the schedule obtained in step 2., by the percentage calculated in step 5.a.ii.</li><li>iv. We recalculated the "credit card discount expense" related to PFCs for 1999 by multiplying the PFC dollars collected via credit card sales, as calculated in step 5.a.iii., by the average credit card discount percentage, as determined by the Company.</li><li>v. We recalculated "bad debt for chargebacks" related to PFCs for 1999 using the Company's methodology and assumptions.</li><li>vi. We summed the credit card discount expense, recalculated in step 5.a.iv., and the bad debt for chargebacks, recalculated in step 5.a.v., for 1999 and agreed the total to the respective amount reported on the Schedule.</li></ol> |
|---------------------|--|



<u>Cost Caption</u>	<u>Procedures</u>
b. Audit Fees (External)	i. We agreed the audit fees reported on the Schedule, to the schedule of Ernst & Young fees for the audit and agreed-upon procedures for 1999.
c. Disclosure Costs	i. We obtained from the Company a schedule of all disclosure cost components related to PFCs for 1999. ii. We agreed the total costs from the schedule obtained in step 5.c.i. to the respective amount reported in the Schedule. iii. We recalculated disclosure costs for 1999, using the Company's methodology and assumptions, which considered the portion of advertising expense attributing to PFCs.
d. Reservations (RSSRs)	i. We obtained from the Company a schedule of all reservations cost components related to PFCs for 1999. ii. We agreed the total costs from the schedule obtained in step 5.d.i. to the respective amount reported in the Schedule. iii. We recalculated reservations expense for 1999 using the Company's methodology and assumptions, which considered, among other things, total reservations calls handled, "PFC" calls handled, seconds per PFC announcement, call hours, average wage rate per hour (including fringe benefits) and telecommunications cost per minute.
e. Passenger Services (CSRs)	i. We obtained from Continental Airlines a schedule of all passenger services cost components related to PFCs for 1999. ii. We agreed the total costs from the schedule obtained in step 5.e.i. to the respective amount reported in the Schedule. iii. We recalculated passenger services expense for 1999 using the Company's methodology and assumptions, which considered, among other things, tickets issued with PFCs, percentage of tickets with PFCs that require manual agent intervention, agent hours worked on manual processing and agent average hourly wage rate (including fringe benefits).
f. Data Entry - Internal, Data Entry – External, Revenue Accounting, Tax Department, and Accounts Payable	<i>Data Entry - Internal</i> i. We obtained from the Company, a schedule of all internal data entry cost components related to PFCs for 1999. ii. We agreed the total costs from the schedule obtained in step 5.f.i. to the respective amount reported in the Schedule.



Cost CaptionProcedures

- iii. We recalculated the internal data entry costs for 1999 based on the Company's methodology and assumptions, which considered estimates of staff and clerical employee time spent entering data related to PFCs and the average wage rate per hour (including fringe).

*Data Entry - External*

- iv. We obtained from the Company a schedule of all external data entry cost components related to PFCs for 1999.
- v. We agreed the total costs from the schedule obtained in step 5.f.iv. to the respective amount obtained in the Schedule.
- vi. We recalculated the external data entry costs for 1999 based on the Company's methodology and assumptions, which considered estimates of the number of PFC documents keyed by the Company's vendor and the cost per document.

*Revenue Accounting*

- vii. We obtained from the Company a schedule of all revenue accounting cost components related to PFCs for 1999.
- viii. We agreed the total costs from the schedule obtained in step 5.f.vii. to the respective amount reported in the Schedule.
- ix. We recalculated the revenue accounting costs for 1999, based on the Company's methodology and assumptions, which incorporated, among other things, estimates of managerial, staff, and clerical employee time spent related to PFCs.

*Tax Department*

- x. We obtained from the Company, a schedule of all tax department cost components related to PFCs for 1999.
- xi. We agreed the total costs from the schedule obtained in step 5.f.x. to the respective amount reported in the Schedule.
- xii. We recalculated the tax costs for 1999, based on the Company's methodology and assumptions, which considered estimates of managerial and staff employee time spent related to PFCs.

*Accounts Payable*

- xiii. We obtained from the Company a schedule of all accounts payable cost components related to PFCs for 1999.
- xiv. We agreed the total costs from the schedule obtained in step 5.f.xiii. to the respective amount reported in the Schedule.



<u>Cost Caption</u>	<u>Procedures</u>
	xv. We recalculated the accounts payable costs for 1999, based on the Company's methodology and assumptions, which considered, among other things, the number of checks distributed and the average cost per check.
g. Corporate Property Department	<p>i. We obtained from the Company a schedule of all corporate property cost components related to PFCs for 1999.</p> <p>ii. We agreed the total costs from the schedule obtained in step 5.g.i. to the respective amount reported in the Schedule.</p> <p>iii. We recalculated the costs for 1999, based on the Company's methodology and assumptions, which considered, among other things, estimates of employee time spent meeting with airports regarding PFCs and travel expenses.</p>
h. Training: Passenger Service (CSRs)	<p>i. We obtained from the Company a summary of all passenger service training costs allocated to PFCs for 1999.</p> <p>ii. We agreed the total costs from the schedule obtained in step 5.h.i. to the respective amount reported in the Schedule obtained in step 1.</p> <p>iii. We recalculated the costs for 1999, based on the Company's methodology and assumptions, which considered, among other things, agent population, average hours of training, and labor rates (including fringe benefits).</p>
i. Internal On-Going IT	<p>i. We obtained from the Company a schedule of all internal ongoing information systems costs allocated to PFCs for 1999.</p> <p>ii. We agreed the total costs from the schedule obtained in step 5.i.i. to the respective amount reported in the Schedule.</p> <p>iii. We recalculated the costs for 1999, based on the Company's methodology and assumptions, which considered, among other things, ongoing costs related to systems support and data storage.</p>
j. CRS On-Going Fees	<p>i. We obtained from the Company, a schedule of all costs related to ongoing maintenance of PFC data for 1999.</p> <p>ii. We agreed the total costs from the schedule obtained in step 5.j.i. to the respective amount reported in the Schedule.</p> <p>iii. We recalculated the costs for 1999, based on the Company's methodology and assumptions which considered the CRS costs related to PFCs.</p>
k. Absorption Cost	<p>i. We inquired of the Company as to which airports it absorbed PFC during 1999.</p> <p>ii. We recalculated absorption cost by multiplying the number of PFCs absorbed by airport, as determined by the Company, by \$3.</p>



<u>Cost Caption</u>	<u>Procedures</u>
	iii. We agreed the total from the calculation in step 5.k.ii. to the respective amount reported in the Schedule.
l. ATPCO	<ul style="list-style-type: none"><li>i. We obtained from the Company, a schedule from ATPCO of estimated annual costs to distribute PFC data to the industry.</li><li>ii. We recalculated the Company's ATPCO costs by multiplying the total industry costs in step 5.l.i. by the Company's estimate of the portion attributed to Continental Airlines.</li><li>iii. We agreed the total from the calculation in step 5.l.ii. to the respective amount reported in the Schedule.</li></ul>
m. ARC	<ul style="list-style-type: none"><li>i. We obtained from the Company, a schedule of all ARC costs incurred in 1999.</li><li>ii. We agreed the total costs from the schedule obtained in step 5.m.i. to the respective amount reported in the Schedule.</li><li>iii. We recalculated the ARC costs for 1999 based on the Company's methodology and assumptions, which considered estimates of the number of PFC documents processed and the processing cost per document obtained from ARC.</li></ul>
n. Interest Revenue	<ul style="list-style-type: none"><li>i. We obtained from the Company a schedule containing the total dollar amount of interest earned on PFC funds held by the Company for the year ended December 31, 1999.</li><li>ii. We obtained from the Company a schedule showing the average number of days that a PFC collected in each month was held from time of receipt by the airline to the time of remittance to the airports or, in the case of refunded tickets, time of refund to the passenger.</li><li>iii. We obtained from the Company a schedule of the average interest rates earned for each month in 1999 on its short-term investment portfolio.</li><li>iv. We recalculated "Interest earned on PFC dollars collected from sales" for the year ended December 31, 1999, by multiplying monthly PFC dollars remitted from the schedule obtained in step 2, by days held (both for remitted PFCs and PFCs refunded to passengers), as a proportion of a 360-day year obtained in step 5.n.ii., and then by the appropriate monthly interest rate percentages obtained in step 5.n.iii.</li><li>v. We agreed the total income for the year, as calculated in step 5.n.iv., to the respective amount reported in the schedule obtained in Step 3.</li></ul>



6. We recalculated the “Cost / PFC Remitted” and the “Cost / PFC Collected” included on the Schedule under the caption “Actual Costs 1999”, by dividing the “Total Costs”, as reported on the Schedule under the caption “Actual Costs 1999” obtained in step 1. (which is net of interest revenue on remitted PFCs as reported in step 3) by the number of PFCs collected and the number of PFCs remitted, as recalculated in step 2.

We were not engaged to, and did not, perform an audit, the objective of which would be the expression of an opinion on the incremental costs included under the caption “Actual Costs 1999” included in the Schedule. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the board of directors and management of the Company and the FAA, and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of the procedures for their purposes. However, this restriction is not intended to limit the distribution of this report, which is a matter of public record.

*Ernst & Young LLP*

December 22, 2000



**Continental Airlines, Inc.**  
**Summary Schedule (1999 Actual, 2000-2002 Forecast)**

	Actual Costs 1999 <sup>1</sup>	1999 Pro-Forma <sup>2</sup>	Implementation Costs <sup>3</sup>	2000* Costs	Full Year Costs 2000 (8A + 8F) <sup>4, 5</sup>	Forecast 2001 <sup>6, 8</sup>	Forecast 2002 <sup>6, 7</sup>
Credit Card Fees	1,687,464	61%		#DIV/0!	1,851,080	67%	
Audit Fees (External)	127,338	6%		#DIV/0!	95,378	3%	
Disclosure Costs	27,000	1%		#DIV/0!	27,540	1%	
Reservations (RSSRs)	433,218	16%		#DIV/0!	445,048	16%	
Passenger Services (CSRs)	133,604	5%		#DIV/0!	134,466	5%	
Data Entry:							
Internal	14,004	1%		#DIV/0!	8,253	0%	
External	3,839	0%		#DIV/0!	3,839	0%	
BSP		0%		#DIV/0!			
Revenue Accounting	128,418	5%		#DIV/0!	147,979	5%	
Tax Department	1,500	0%		#DIV/0!	1,528	0%	
Accounts Payable	38,516	1%		#DIV/0!	38,991	1%	
Corporate Property Dept	41,375	2%		#DIV/0!	43,025	2%	
Training:							
RSSRs		0%		#DIV/0!			
Data Entry		0%		#DIV/0!			
Passenger Service (CSRs)	336,711	12%			339,081	12%	
Internal One-Time IT update		0%	147,280	100%	#DIV/0!		
Internal On-Going IT	64,093	2%			65,501	2%	
CRS One-Time update		0%		0%	#DIV/0!		
*CRS On-Going fees	81,618	3%			82,532	3%	
ATPCO	764	0%			764	0%	
ARC	38,593	1%		0%	#DIV/0!	41,192	2%
Interest Revenue	(424,207)	n/a			n/a	(544,186)	n/a
<b>TOTAL COSTS</b>	<b>2,744,844</b>	<b>116%</b>	<b>147,280</b>	<b>100%</b>	<b>#DIV/0!</b>	<b>2,792,011</b>	<b>100%</b>
<b>Number of PFCs Remitted</b>	<b>30,133,012</b>	<b>30,133,012</b>	<b>30,133,012</b>		<b>31,188,509</b>	<b>32,103,584</b>	<b>33,066,871</b>
<b>Number of PFCs Collected</b>	<b>33,065,353</b>	<b>33,065,353</b>	<b>33,065,353</b>		<b>35,480,338</b>	<b>38,524,148</b>	<b>37,819,870</b>

Cost / PFC Remitted	\$0.0911	\$0.0049	#DIV/0!	\$0.0896	\$0.0898	\$0.0893
YOY Change			#DIV/0!	-1.7%	0.3%	-0.6%
Cost / PFC Collected	\$0.0830	\$0.0045	#DIV/0!	\$0.0787	\$0.0790	\$0.0785
YOY Change			#DIV/0!	-6.2%	0.3%	-0.6%

Absorption Cost	\$8,345,955	\$0.0000		\$8,828,730	\$9,031,791	\$9,239,522
Cost / PFC Remitted (including Absorption)	\$0.3681		\$0.0000	\$0.3728	\$0.3712	\$0.3687
Cost / PFC Collected (including Absorption)	\$0.3254		\$0.0000	\$0.3277	\$0.3262	\$0.3241

ASM growth rate	2.2%	2.3%	2.2%
*CPI - Urban* from WEA <sup>9</sup>	3.3%	2.4%	2.4%

- Notes:
- 1 - Actual costs incurred. Costs have been agreed upon by an independent auditor.
  - 2 - Assumes the same volume as 1999, but with 100% of PFCs Collected at \$4.50 per PFC -- this only impacts Credit Card Fees and Interest Revenue.
  - 3 - For any costs associated with the implementation of the new maximum \$4.50 PFC rate. This column is not year specific.
  - 4 - [10-11] months of 2000 are actual with [1-2] months of forecast
  - 5 - Does not include any Implementation Costs
  - 6 - Assumes 3 months with 100% of PFCs Collected at \$3. Assumes 9 months with 50% at \$3 and 50% at \$4.50.
  - 7 - Assumes 12 months with 100% of PFCs at \$4.50.
  - 9 - .005 - This is an estimated percentage of the compilation required for PFC verses all other computations for a booking transaction.

For any carrier specific "issues"